



STATE WATER PROJECT CONTRACT EXTENSION PROJECT

Draft Meeting Summary and Action Items

State Water Project Contract Extension Project

June 26, 2013 10:00 AM – 3:00 PM

Draft Meeting Attendance List

California Department of Water Resources Lead Negotiators

- Carl Torgersen, California Department of Water Resources
- Steve Cohen, California Department of Water Resources
- Rob Cooke, California Department of Water Resources
- Perla Netto-Brown, California Department of Water Resources
- Vera Sandronsky, California Department of Water Resources
- Ralph Torres (by phone), California Department of Water Resources

State Water Project Contractor Lead Negotiators

- David Aladjem, Alameda County Flood Control and Water Conservation District, Zone 7
- Dan Flory, Antelope Valley-Eastern Kern Water Agency
- Paul Gosselin, Butte County
- Valerie Pryor, Castaic Lake Water Agency
- Curtis Creel, Kern County Water Agency
- Mark Krause, Desert Water Agency
- Kathy Cortner, Mojave Water Agency
- Steve Arakawa, MWD of Southern California
- Deven Upadhyay, MWD of Southern California
- Bob Perreault, Plumas County Flood Control & Water Conservation District
- Douglas Headrick, San Bernardino Valley Municipal Water District
- Jeff Davis, San Geronio Pass Water Agency

- Matt Naftaly, Santa Barbara County Flood Control & Water Conservation District
- Ray Stokes, Santa Barbara County / Central Coast Water Authority
- Joan Maher, Santa Clara Valley Water District
- David Okita, Solano County Water Agency
- Mark Gilkey, Tulare Lake Water Storage District and County of Kings
- Lisa Kern (by phone), Ventura County Flood Control District
- Steve Wickstrum (by phone), Ventura County Flood Control District

California Department of Water Resources Staff

- Ted Alvarez, California Department of Water Resources
- Mark Andersen, California Department of Water Resources
- Lauren Bisnett, California Department of Water Resources
- Cathy Crothers, California Department of Water Resources
- Terri Ely, California Department of Water Resources
- Karen Enstrom, California Department of Water Resources
- Jennifer Iida, California Department of Water Resources
- Scott Jercich, California Department of Water Resources
- Spencer Kenner, California Department of Water Resources
- Kathie Kishaba, California Department of Water Resources
- Chris Martin, California Department of Water Resources

<ul style="list-style-type: none"> Philip LeCocq, California Department of Water Resources Dave Paulson, California Department of Water Resources David Sandino, California Department of Water Resources Nancy Quan, California Department of Water Resources Dena Uding, California Department of Water Resources Pedro Villalobos, California Department of Water Resources <p><u>State Water Project Contractors and SWC, Inc.</u></p> <ul style="list-style-type: none"> Gary Bucher (by phone), Kern County Water Agency Eric Chapman, State Water Contractors, Inc. Jaime Dalida, MWD of Southern California Kevin Donhoff, MWD of Southern California Terry Erlewine, State Water Contractors, Inc. Amparo Flores, Alameda County Flood Control and Water Conservation District, Zone 7 Tom Glover, Dudley Ridge Water District Lynn Hurley, Santa Clara Valley Water District Dana Jacobson, Santa Clara Valley Water District Theresa Lightle, State Water Contractors, Inc. Don Marquez, Kern County Water Agency Amelia Minaberrigarai, Kern County Water Agency 	<ul style="list-style-type: none"> Josh Nelson, Best, Best & Krieger LLP/Crestline Lake Water Agency Ted Page, Kern County Water Agency Julie Ramsay, State Water Contractors, Inc. David Reukema, MWD of Southern California John Schlotterbeck, MWD of Southern California Cliff Schulz, State Water Contractors, Inc. Leah Wills, Plumas County Flood Control and Water Conservation District <p><u>DWR Consultants for Contract Extension</u></p> <ul style="list-style-type: none"> Erick Cooke, Environmental Science Associates Barbara McDonnell, MWH Global <p><u>Public</u></p> <ul style="list-style-type: none"> Stan Dirks, Orrick, Herrington & Sutcliffe LLP Mike Nelson, Dublin – San Ramon Services District; Bold, Polisner, Maddow, Nelson & Judson Patricia Schifferle, Planning & Conservation League <p><u>Facilitation Team</u></p> <ul style="list-style-type: none"> Alex Braunstein, Kearns & West Charlotte Chorneau, Kearns & West Kelsey Rugani, Kearns & West Anna West, Kearns & West
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I. Welcome/Introductions

There were roundtable introductions of the negotiation teams and staff. Members of the public were given the opportunity to introduce themselves.

II. Meeting Overview

Anna West reviewed the Meeting Ground Rules emphasizing respect and listening. She also reviewed the process for public comment at the end of the meeting. Anna outlined the negotiation session agenda and stated that SWP Contractors Contract Offer will be discussed.

Anna then reviewed the action list from the May 29, 2013 negotiation session. All of the action items have been completed except for convening a Technical Team to address 1hh; this is an ongoing task. The group finalized the May 29 Meeting Summary, which will be posted on the website.

III. SWP Contractors Contract Offer

Before the SWP Contractors reviewed their offer, Carl asked how the proposal was consistent with DWR's and SWP Contractors' objectives and how it originated. Carl also shared that he has met with the Director who affirmed that Objective 2b needs to be a part of this current negotiation and he emphasized its importance to DWR.

David Okita reviewed the proposal development process, which began over a year ago. SWP Contractors held workshops to become familiar with the process and terminology. David mentioned that although Butte County and Plumas County Flood Control and Water Conservation District did not participate in the workshops since they are not members of the State Water Contractors, Inc., they have been involved in the recent caucuses. He clarified that the SWP Contractors offer will be reviewed and discussed today has been shared with all 29 Contractors and there were no objections heard.

No Contractor has presented objections to the counter offer proposal. David clarified that counter offer does not mention Objective 2b and that this was intentional. The Contractors believe there are important financial issues that will need to be discussed over time with DWR. From the Contractors' perspective, these topics include 2b, Davis-Dolwig costs, 1hh, and how to handle excess revenue.

Ray Stokes then presented the SWP Contractors offer and outlined its key points. The Contractors proposed extending the contract 75 years through 2110. DWR's initially offered a 40 year contract through 2075. The Contractors also recommend eliminating the contract term which provides that DWR may issue revenue bonds beyond the term of the contract ending with the latest maturity date of any bond issued.

Regarding Objective 3, Ray explained that costs incurred between 1961 and 2015, termed "Legacy Year Costs," will be billed under a Freeze-Go system. Reimbursement would remain consistent with current contract terms for all costs incurred prior to the implementation date as defined by an Amendment. "Post-Legacy Year costs," or those costs incurred between 2016 and the end of the next contract term, would be billed with a Pay-As-You-Go method, so that the Contractors will annually pay for actual and estimated costs as well as debt service (i.e., principle, bond payments are included; there is no project interest rate).

SWP Contractors offered eliminating the Project Interest Rate under- and overpayments on costs incurred from January 1, 2016 to the term of the contract, as well as eliminating the Replacement Accounting System (RAS). The Contractors believe that this accounting system would be inconsistent with a Pay-As-You-Go Method. Ray mentioned that SWP Contractors would like to further discuss how 51(e) revenues are allocated and that these funds need to benefit all of the Contractors proportionately. The Contractors also recommended that the Water System Revenue Bond Surcharge be terminated at the end of the Project Repayment Period.

Ray then reviewed the three offers that combined are the Contractors offer to address Objective 2a. Regarding the General Operating Reserves Account (GOA), the Contractors proposed increasing the reserves amount to \$60 million provided by excess revenues for cash flow deficiencies resulting from chargeable water supply purposes. They recommended eliminating the adjustment authorized after 2001 increasing the GOA account to \$60 million. The Contractors proposed establishing GOA funding as a superior priority to other SWRDS purposes and subordinate to rate management. Additionally, the

Contractors offered eliminating the Contractors' 30 Day Grace Period, which would give DWR an additional \$40 million in cash flow, according to SWP Contractor estimates. Also, the Contractors offer includes increasing the annual rate reduction to \$48 million, subsequent to the PMIA Loan Payoff. This could then be used as authorized supplemental billing which the Contractors estimate can be obtained within 30 days. SWP Contractors also propose that SWRDS be authorized to refund GOA Investment Earnings annually.

Ray provided an overview of how the SWP Contractors foresee organizing financial management of the State Water Resources Development System. They suggest having a Chief Financial Officer (CFO) who would have primary oversight of SWRDS. The CFO's department would be responsible for creating an annual financial plan on which the contract is based and providing monthly reports to the Contractors. The financial plan would be subject to review by a committee of both Contractors and DWR management. Lastly, Ray summarized that their GOA offer was equivalent to 90 days of operating and power costs to equal \$148 million including the \$60 million in reserves, \$48 million in cash within 30 days from supplemental billing, and \$40 million that would be the result of eliminating the 30-day grace period.

IV. AIP Package Continued

Carl thanked the Contractors for all of their effort in putting together the counter offer. Initially, some of the items were not particularly positive from DWR's perspective. Additionally, DWR hoped to reach agreements as rapidly as possible and there is concern that things have been added to the discussion that will hinder completing the Contract Extension Process in a timely manner. DWR agrees that some issues will need to be discussed later on and/or through a different venue, but he clarified that 1hh and Objective 2b are both imperative to include in the overall concept of reserves through this current effort. DWR agrees that Davis-Dolwig can be addressed at a later time. Perla Netto-Brown clarified that DWR's proposal included needing 120 days of operating and power costs, not 90 days.

DWR then commented and asked a series of clarifying questions on the SWP Contractor offer presentation, and the Contractors responded.

Term of Contract

- Extend Contract Term by 75 Years to December 31, 2110
- Eliminate the Contract Term Ending with the Latest Maturity Date of Any Bond Issued

Repayment of "Such Facilities" – Latest Bond Maturity Date

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DWR Comment: DWR's position at this point is that other issues need to move further before the Contract term is decided.

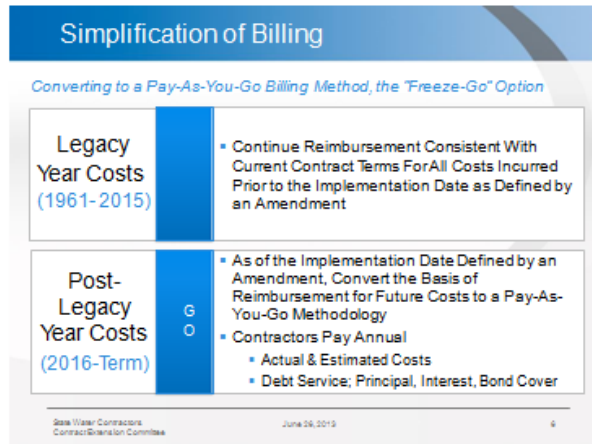
DWR Question: What is the purpose of eliminating the provision in the contract to have it extended if DWR were to sell bonds on the project?

SWP Contractors Answer: The Contractors have perceived that DWR is not favorable to that provision of the Contract and that it is not necessary.

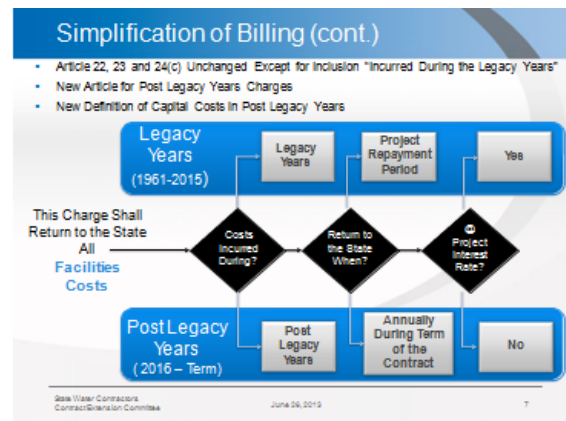
DWR Comment: The Contractors believe that the Department wants to eliminate this?

SWP Contractor Comment: Yes.

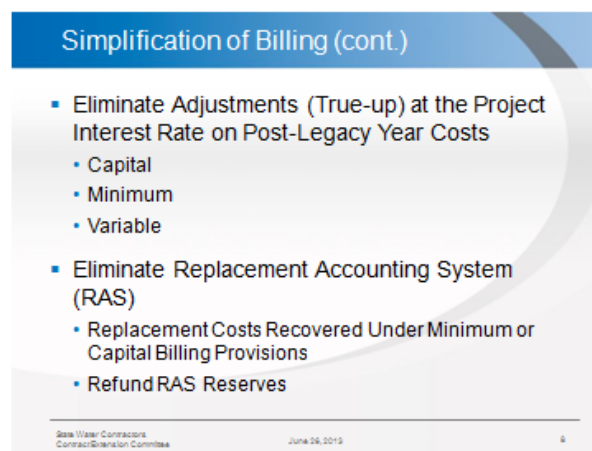
DWR Comment: We see this as a safety valve as we approach the near end of a project and this action would increase flexibility in extending the Contract if needed.



DWR Question: Clarifying that Legacy Year Costs will be paid under Freeze-Go? The word "Freeze" was not included, is there a reason?
SWP Contractors Answer: That was not intended. Legacy Year Costs would be paid under Freeze-Go.



DWR Question: What does the third bullet, "New Definition of Capital Costs in Post Legacy Years" mean? What about conservation minimum?
SWP Contractors Answer: As it exists currently, Contractors pay all costs to DWR regardless of how the project is funded. The intention is not to omit conservation minimum costs. The plan would be that conservation minimum costs would go to Pay-As-You-Go.
DWR Comment: Not sure how the Contract language would need to change after 2016.
SWP Contractors Comment: Let's address this in a Technical Team.



DWR Question: On the first bullet, does it eliminate the application of adjustments at the project interest rate or does it mean that adjustments are eliminated?
SWP Contractors Answer: We mean to eliminate the application of adjustments at the project interest rate.
DWR Question: Would you eliminate the application of capital costs?
SWP Contractors Answer: This has not been discussed yet.
DWR Comment: On the "Eliminate Replacement

Accounting System (RAS)" bullet, this was not considered when DWR projected the GOA amount. This issue needs to be discussed by the Technical Team to determine if we should consider this, and if considered, it may impact the need to increase the GOA account.

General Operating Reserves (GOA)

- Increase GOA to a Maximum of \$60M From Excess Revenues
 - Eliminate Adjustment Authorized After 2001
- Establish GOA Funding Priority:
 - Superior to Additional System Purposes
 - Subordinate to Annual Rate Reductions
- Subsequent to PMIA Loan Payoff:
 - Increase Annual Rate Reductions to \$48M
 - Eliminate Restricted GOA Annual Funding Rate of \$2M, Allowing Funding to \$60M Cap from Excess Revenues

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DWR Comment: Our proposal set the GOA at 120 days. Are we correct that the SWP Contractors offer tries to achieve 90 days? Also, to clarify, DWR does not believe that addressing variability addresses the department's cash reserve needs.

SWP Contractors Comment: Yes, the \$148 million identified in slide 11 achieves an equivalent of 90 days.

DWR Question: Is the proposed GOA \$60 million a fixed amount?

SWP Contractors Comment: Another part of the proposal relates to fiscal management and changes made within DWR to improve fiscal management.

The reserves will be set initially at \$60 million, but increases will be tied to milestones reached in fiscal management. These milestones have not been discussed yet.

General Operating Reserves (GOA) (cont.)

- Authorize GOA for Any Cash-flow Deficiencies Resulting from Chargeable Water Supply Purposes
- Eliminate Contractors' 30 Day Grace Period
- Authorize SWRDS to Refund GOA Investment Earnings

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DWR Question: Can the first bullet be clarified?

SWP Contractors Answer: The Contractors have had discussions about the potential use of the GOA as it currently exists. Currently, there are limitations on how to use the GOA with cash deficiencies from DWR. The Contractors want to ensure that there are not restraints to accessing that account, particularly in an emergency.

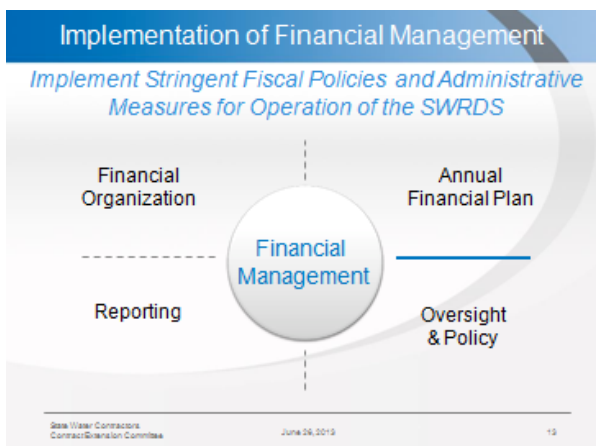
DWR Question: Are the Contractors saying that the GOA can be used for water supply purposes only? What about for an emergency like Thermalito?

SWP Contractors Answer: Yes, the GOA can be used for water supply purposes, but not for non-

reimbursable costs. Up until 2035, there will be 51(e) revenues that could be used for those types of costs.

DWR Question: Can it be used for all billing components – transportation, conservation, etc.?

SWP Contractors Comment: Yes.



DWR Question: Can you define "improved fiscal management"?

SWP Contractors Answer: Components of improved fiscal management are outlined on this slide. It could change over time, but milestones should be established to ensure that improvements are being made. Setting up a separate office for SWRDS only,

or providing annual budgets are examples of possible milestones.

DWR Comment: DWR supports improving the financial management of the State Water Project. Perhaps to the extent that these factors can be implemented, it may be more appropriate to discuss this in an administrative venue. These will take time to implement, if agreed upon, and a continued conversation about these items is suggested as a next step.

SWP Contractors Comment: This issue relates to 2.3.4 of the counter offer proposal, which is broader than just financial management. There is concern that if this issue is taken up in an administrative setting, the commitment might not be upheld or sustained over time.

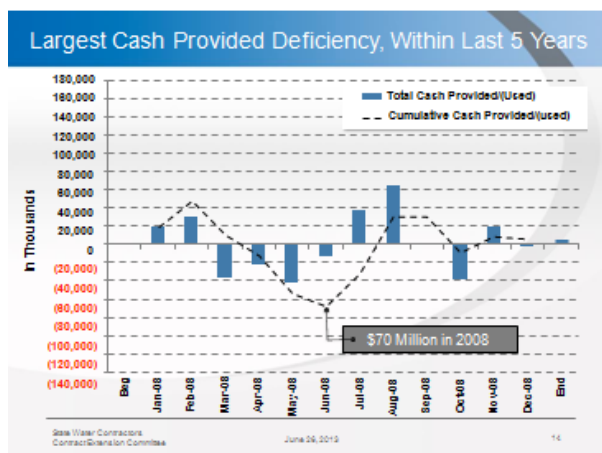
Summary of GOA Offer			
Equivalent to 90 Days of Operating and Power Costs or \$148 Million			
Cash-Flow Tools	Reduction in Deficiency Of Net Cash Provided	Cash	Cash Within 30 Days
Elimination of 30-Day Grace Period	40		
Reserve Amount		60	
Authorized Supplemental Billing			48

DWR Comment: DWR would like to take a closer look at some of the numbers proposed. For example, a Technical Team should review how elimination of a 30-day grace period equals the \$40 million level. Currently, there is \$32 million in the Replacement Accounting System and the current GOA is \$27 million. The RAS and GOA accounts add up to \$60.3 million total currently. The counter offer proposal would provide \$60 in the GOA giving DWR a loss of \$0.3 million. It may look like the reserves account will have less money, but the money available by eliminating RAS would need to be added to reserves.

SWP Contractors Comment: The RAS is not allowed to be used currently for emergency situations. The Contractors are looking at DWR's financial needs from two perspectives: to reduce variability (by eliminating the grace period, and providing opportunities for subsequent billings, etc.) and by providing DWR with tools for how to deal with variability (i.e., reserves).

DWR Comment: That is how DWR currently operates. The types of charges would not change except DWR would be giving up the workable capital account that currently exists. Less cash may be available.

SWP Contractors Comments: The proposal was not developed quickly or without a lot of thought. It was developed based on analysis of what the underlying issues are. The Department is not a utility because it has a guaranteed stream of revenue. These are the primary reasons for the concepts in our offer.



DWR Question: Did this chart inform the offer?

SWP Contractors Answer: Yes, this comes from previous DWR presentations. It illustrates that there were two timing issues that need to be dealt with: liquidity and emergency situations. All organizations represented here have a budget. If it looks like something is going to go over, something is changed to mitigate that. As the year progresses, the financial reports will show if DWR is about to go over and they can mitigate. For emergency situations, there will be a true cash reserves of about \$108 million.

DWR Question: Do the Contractors see extending

supplemental billing after 2035?

SWP Contractors Answer: Extending supplemental billing has not been thought about and how it relates to rate management. There will not be rate management efforts in 2036 so this should be discussed by a Technical Team.

Following the series of questions, answers and comments, DWR and the Contractors began discussing how the process will move forward. Additional discussion will occur on Objective 2a and 3 in a Technical Team meeting including discussion of 1hh, non-reimbursable costs, and the equitable allocation of 51(e) revenues. Since Objective 2b is a larger policy issue and discussion has focused primarily on concepts rather than details thus far, DWR will develop and distribute a proposal on Objective 2b.

V. Next Steps

Anna reviewed the Contract Extension Process Schedule, including three negotiation dates that will be needed, and mentioned that BDCP Participation Options will be discussed at the negotiation on July 10th. Anna reviewed the action items.

VI. Public Comment

Patricia Schifferle from the Planning & Conservation League provided oral comment.

VII. Adjourn

The meeting was adjourned.

Action Items		Responsibility Due Date
1.	May 29 Negotiation Session Meeting Summary to be finalized and posted on website.	Kearns & West ASAP
2.	Objective 2a and Objective 3: Convene a Technical Team to discuss: (1) "Definition of Capital Costs" for this contract; (2) the State Water Contractor's proposal to eliminate the Revenue Accounting System (RAS); (3) review the assumptions and estimated values in the Contractor's GOA Offer (slide 15), including the elimination of the 30-day grace period, the reserve amount, and authorized supplemental billing process and timing; (4) use of the reserves (SWP Contractor's proposed only use for water supply purposes); (6) equitable allocation of 51(e) (pie chart, slide 9); and, (7) 1hh.	Perla Netto Brown, Rob Cooke and Ray Stokes July 8 th 2:00pm – 5:00pm and July 9 th 1:30pm – 4:30pm
3.	Financial Concepts. a. DWR will internally discuss the SWP Contractors proposal to capture financial management concepts through this Contract Extension process. b. DWR and SWP Contractors to form an administrative committee on budgeting and to review current reporting processes.	Carl Torgersen July 10 th Carl Torgersen and Curtis Creel

		Prior to July 10 th
4.	DWR Counter Offer. DWR will prepare a counter offer package proposal to review at the next Negotiation Session.	Carl Torgersen/DWR Team On or Before July 10th
5.	Objective 2b: DWR will develop and distribute a proposal on Objective 2b. The proposal will address the amount and processes associated with 2b.	Steve Cohen and Scott Jercich July 8th
6.	SWP Contractors will prepare an offer on the BDCP Objective; K&W to distribute to all.	Paul Gosselin and Kearns & West July 8th
7.	June 26 Negotiation Session Meeting Summary to be prepared.	Kearns & West ASAP